

Duane Catlett Testimony in support of SB374

Mr. Chairman and members of the Senate Taxation Committee,

My name is Duane Catlett.

I am a private Montana citizen, and I rise to strongly support the passage of SB374.

I am a retired PhD nuclear scientist and an expert on design and fabrication of advanced sophisticated materials that must perform without failure for long term (40 years and beyond) energy production applications under extreme hot and cold temperatures and corrosive environmental conditions. I have managed several multimillion dollar projects and organizations during my career. I understand how the financial management and dynamics of large successful organizations work in both corporate and government worlds.

My education background and business experience tells me that the existing oil and gas tax holiday is a very bad deal for the people of Montana, and it needs correction.

My interest in oil and gas extraction comes because of the extreme stress that the drilling and fracking operations exert on the drilling environment and on the impacted communities and their citizens. It is one thing to provide incentives for businesses to move to Montana to advance sustainable growth in our main street economy; it is quite another thing to give away our non-renewable treasure to outside corporations that will only invest the additional profits realized by the tax holiday outside our state's borders.

We Montanans are rightly proud of our Treasure State. But we are keenly aware of the fact that natural resource extraction is always a boom – bust economic cycle. The big difference with oil and gas extraction from "Tight Oil" formations, like the Bakken, is that the bust will arrive much sooner than those of the conventional vertical oil wells of the past.

When the drilling music stops, the impacted communities will be left holding the bag. Montanans know from experience what ghost towns look like and how quickly communities expanded to accommodate the oil boom can return to dust*.

Corporations profiting from our nonrenewable resource must be held responsible for financing the community infrastructure required to support their profit generating endeavors.

The production definitions in the tax holiday legislation is needlessly complex and does not realistically or technically define the extraction processes as we know them to be after eight to nine years of "Tight Oil" production. So, here are some facts.

The Bakken oil play consists of horizontal drilling and subsequent hydraulic fracturing (fracking) of the shale formations to release the oil held tightly in the shale pores. The fracking provides interconnectivity of the pores to allow the trapped oil to escape to the wellbore to be pumped to the

surface. But the very nature of tight oil formations limits the total volume of oil that can be released per fracture event, and it is rapidly depleted.

Extraction of oil from “Tight Oil” formations like the Bakken consists of a two stage process, the drilling of the well’s vertical and horizontal shafts followed by hydraulically fracturing, or “fracking,” about 5,000 to 10,000 feet of the horizontal pipe into 20-30 stages. Each fracked stage releases the oil contained in that fracture zone. That finite quantity of oil is extracted quickly in comparison to conventional vertical wells of the past.

Traditional vertical wells in conventional porous oil pools typically take two years to decline 50 percent to 55 percent, and they can keep pumping for 20 years or more. But, after the past eight to nine years of hydraulic fracturing production, we know that production from individual wells drilled into “Tight Oil” formations decline by 60 percent to 70 percent in the first year alone and that the decline lines for all individual fracked wells follow the same decline rate (**Figure 1**). Tight Oil production wells are depleted another 20% to 30% by end of the third year and the remaining production after three to five years is down to a trickle.

About 70% of each new well’s total lifetime production has been given away tax free in the first year of production.

Opposition lobbyists will tell you that the production will last much longer, but here’s the deal. Maintaining or increasing production rates in Tight Oil formations, requires that a well’s horizontal zone be drilled to additional lengths and new stages fracked, or new vertical wells have to be drilled. Operational limits restrict the number of wells to one to three wells per square mile. All of this data shows that we have already gifted roughly 40% of the total tight oil existing in Montana’s oil formations to the oil producers.

The tax holiday is very bad deal for Montana taxpayers. Each well’s production should be taxed from production day 1.

Figure 2. shows that the short productive lifetime of a “Tight Oil” well means that peak oil production of tight oil formations, like the Bakken, is right around the corner, projected to be reached in 2015.

It looks like the “black gold” rush boom to bust cycle might not last nearly as long as SB374 opponents would ask you to believe, and when the drilling music stops the impacted communities will be left “without a chair to sit on.” Montanans know what ghost towns look like and how quickly communities expanded to accommodate the oil boom can return to dust*.

Adding insult to injury, existing property rights law gives superiority of the mineral rights owner over the surface owner, so that the drillers can drill almost on top of the surface owner’s house and compromise his water sources leaving the surface owner with no recourse to justice.

The corporate lobbyists opposing this bill will also claim that without the tax holiday, they will take their business elsewhere. The fact is that Montana’s Tight Oil formations are a valuable finite resource, and if

the free market doesn't justify extraction at this time the right decision for the State is to wait until the market price justifies the producers coming after it.

That's just sound business. That's the way the free market should work. We must not give away our oil assets. At some point in time the markets will change and corporations will find it profitable to again drill in Montana and do it while paying a fair tax rate.

Here are the business facts.

Oil and Gas corporations will only drill where there is oil and when it is profitable at market prices. Montana must set its tax rates for nonrenewable resources at a fair value and that rate then becomes only one of the expenses that industry must include in its production financial planning. If it makes business sense, they will drill in Montana; and if it doesn't make business sense, they will not.

I don't need to remind anyone that we operate as a free market, so if corporate profit objectives are met, they will drill; and if it is not profitable, they will not drill. We do not serve Montana well if we give away our nonrenewable resources for free. At some point economics will turn in our favor. Our legislators should set a fair tax rate and let the free market price of crude determine the timing of extraction.

You, as our legislators, will vote on SB374 either to protect profits for the corporate friendly oil and gas tax holiday give-away, or you will vote to protect the economic freedom of individual Montanans. That is the choice you will make.

The United States Constitution was written by the Founders to form a government of, for, and by the people. Corporations were subsequently formed to do the work in support of the people, not the other way around. The corporations are responsible for providing the funding for the impacted communities' infrastructure needs, not the Montana taxpayers.

The right vote on this bill should be obvious. Your job as legislators is to protect the individual freedoms of Montana citizens. It is not to protect the profits of oil and gas industry owners.

Continuing the oil and gas holiday as currently structured makes no ethical or business sense. A vote for continuing the current oil and gas tax holiday is a vote for the industry lobby.

I strongly urge you to support SB374. Thank you for allowing me to testify today.

* From Bloomberg Business:

"Oklahomans know about oil boom bubbles. In the Osage Nation, a tribal territory, derelict oil pumps rust away on the prairie, part of the Burbank oil field. Discovered in 1920, the field saw its production peak in 1923 at a daily average of 72,000 barrels. A town of thousands, including 300 businesses, sprang up. The locals called it Whiz-bang. Today, other than a few farmhouses and a street sign, Whizbang has vanished into the grass."

Figure 1.

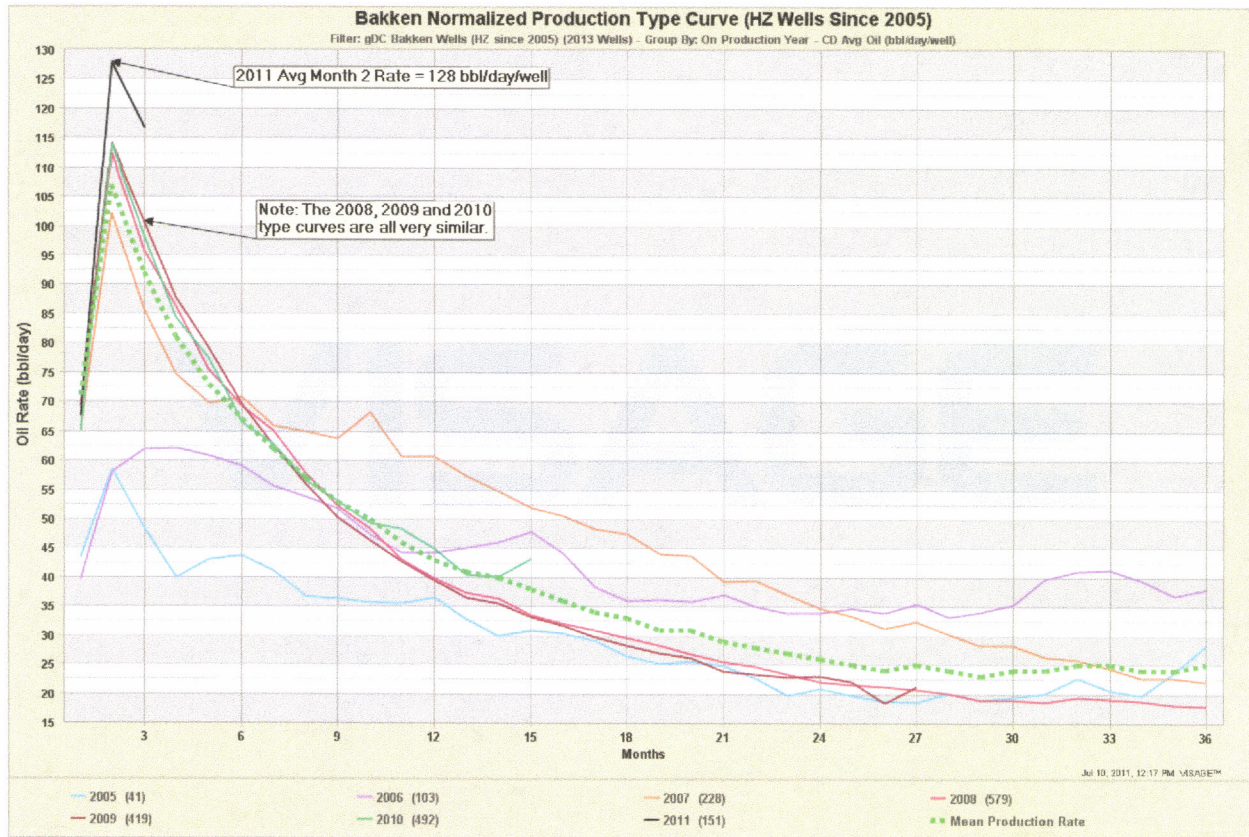


Figure 2.

